Beyond Issuers: The Future of Private Securities Litigation

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Private securities litigation has traditionally been viewed as a subfield of corporate governance, reducing agency costs by disciplining wayward management. In this brief Symposium essay, I argue that the future of private securities litigation lies beyond issuers. I discuss how a fraud claim under Rule 10b-5 can be understood as a kind of economic tort, and set out, in broad strokes, an economic analysis of claims against non-issuer defendants. I then consider emerging trends in the case law against non-issuers in social media and market manipulation cases. I conclude by identifying some challenges and opportunities for securities litigation in a "beyond issuer" era.

I. INTRODUCTION

Thanks very much to the *Journal of Corporation Law* for the opportunity to contribute to such a timely Symposium on the future of corporate and securities law. In this brief essay, I offer a few thoughts on the future of private securities litigation. I begin with the observation, which I hope is not terribly controversial, that private securities litigation, like securities regulation more broadly, was often viewed as highly adjacent to, if not a direct subfield of, corporate governance.[1] The classical literature tended to justify mandatory securities disclosure by pointing to the social welfare gains from share price accuracy in the

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1. *See, e.g.*, David H. Webber, *Private Policing of Mergers and Acquisitions: An Empirical Assessment of Institutional Lead Plaintiffs in Transactional Class and Derivative Actions*, 38 DEL. J. CORP. L. 907, 920 (2014) ("The purpose of private securities and transactional litigation is to provide shareholders with a tool for policing a broad range of managerial misconduct.") (citing Robert B. Thompson & Randall S. Thomas, *The New Look of Shareholder Litigation: Acquisition-Oriented Class Actions*, 57 VAND. L. REV. 133, 144 (2004)).

form of reduced agency costs and better resource allocation when firms raised capital.[2] In short, by deterring fraud, private securities litigation like other forms of shareholder litigation, promoted good governance.

This traditional framework can be understood as a kind of regulation of the investment contract between shareholders and managers. The problem with allowing issuers to opt out of securities disclosure, scholars argued, was that they would rationally contract for a privately optimal level of disclosure that fell short of the socially optimal level.[3] Just like how regulation is more broadly justified because of the impact on nonparties to a contract, mandatory rules are more likely to produce the socially optimal level of disclosure.[4] And because rules are largely useless without enforcement, securities litigation in general—and private class actions in particular—are similarly justified as a means of ensuring that contracts between issuers and investors produce the socially optimal level of accurate information in the market.[5]

This is an incomplete picture. The private right of action for Rule 10b-5—the chief antifraud provision of the federal securities laws—certainly has its roots in a bygone era of judicial activism which looked favorably on plaintiffs as private enforcers of regulatory mandates alongside government agencies like the Securities and Exchange Commission.[6]

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2. *E.g.*, Merritt Fox, *The Issuer-Choice Debate*, 2 THEORETICAL INQ. L. 563, 582 (2001) (finding that "[t]he social benefits of disclosure are improved capital allocation and lower agency cost of management."); Zohar Goshen & Gideon Parchomovsky, *The Essential Role of Securities Regulation*, 55 DUKE L.J. 711, 720 (2006) ("Accurate pricing is also important to the market for corporate control, for monitoring and controlling the management agency problem, and for the allocation of resources through initial public offerings and secondary offerings."); *see also id.* at 748 ("In addition to facilitating a competitive market for information traders, securities regulation complements corporate law in reducing management agency costs."). Literature on entrepreneurial plaintiffs' firms also embraced the agency-cost framework. *See, e.g.*, John C. Coffee, Jr., *Accountability and Competition in Securities Class Actions: Why "Exit" Works Better than "Voice"*, 30 CARDOZO L. REV. 407, 407–08 (2008) (contrasting "litigation governance" with corporate governance more broadly).

3. *E.g.*, Fox, *supra* note 2, at 564 ("Issuer choice would lead to a significant market failure arising from the fact that each issuer's private costs of disclosure would be greater than the social costs of such disclosure."); Goshen & Parchomovsky, *supra* note 2, at 756 ("[B]ecause the corporation can neither charge for these benefits nor exclude nonpaying parties from using the information, the corporation will under-disclose information. In fact, each corporation would prefer to free ride on the benefit generated by the disclosure of other corporations and minimize its own disclosure. In sum, the misalignment between the private and social value of information justifies mandatory disclosure.").

4. *E.g.*, Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice is Not Investor Empowerment*, 85 VA. L. REV. 1335, 1338–39 (1999) ("For each U.S. issuer, there is a socially optimal level of disclosure . . . [which] is reached when the marginal social benefits equal the marginal social costs . . . issuer choice [on disclosure requirements rather than mandatory rules] would lead U.S. issuers to disclose at a level significantly below this social optimum."); John C. Coffee, Jr. *Market Failure and the Economic Case for a Mandatory Disclosure System*, 70 VA. L. REV. 717, 728 (1984) ("[C]ontractual problems, in combination with the public goods nature of securities research, help explain how a mandatory disclosure system benefits investors. Put simply, if market forces are inadequate to produce the socially optimal supply of research, then a regulatory response may be justified.").

5. *See* Merritt B. Fox, *Why Civil Liability for Disclosure Violations When Issuers Do Not Trade*, 2009 WIS. L. REV. 297, 317–18 (articulating why a private damages regime can effectively supplement public enforcement of misstatements); *see also* Rafael La Porta, Florencio Lopez-De-Silanes & Andrei Shleifer, *What Works in Securities Law?*, 61 J. FIN. 1 (2006) (presenting an empirical study from across 49 countries showing strong evidence that the presence of privately-enforceable mandatory disclosure laws is beneficial to markets).

6. *Cf.* J.I. Case Co. v. Borak, 377 U.S. 426, 432 (1964) ("Private enforcement of the proxy rules provides a necessary supplement to Commission action.").

But Rule 10b-5 also provides redress for injury caused by one market participant to another in settings where the regulation of issuer disclosure was largely irrelevant. For example, courts have recognized private fraud claims against issuers where a third-party market maker sold a derivative security at an inflated price to a third-party purchaser[7] or market manipulation claims by hedge funds against market makers.[8] It is difficult to see how the aggregate out-of-pocket loss from third-party contracts bears any connection to the optimal level of issuer disclosure.[9] Rather, these claims seek redress for deceit that caused economic harm to a counterparty. In a word, an economic tort.

The following Parts discuss this tort-like justification for private securities litigation as a means of redressing economic harms caused by one party deceiving another, where there exists no contract between the parties. Part II briefly sketches out some conceptual points for a tort-like view of securities law. Part III considers the rise of non-issuer private securities litigation in the courts. Part IV offers concluding thoughts.

II. NON-ISSUER SECURITIES FRAUD: CONCEPTUAL FOUNDATIONS

A. Securities Fraud as an Economic Tort

The characterization of Rule 10b-5 claims as an economic tort, rather than one akin to a shareholder claim brought under state corporate law, should not be particularly controversial.[10] The rule prohibits *any person* from engaging in fraud in connection with the purchase *or sale* of a security. On its face, this language has little to do with shareholder rights and contemplates a broader set of plaintiff-defendant pairs than shareholders suing issuers. Besides the obvious point that the SEC regularly brings Rule 10b-5 claims against non-issuer defendants,[11] courts have allowed Rule 10b-5 claims to be brought by private

7. *See, e.g.*, Deutschman v. Beneficial Corp., 841 F.2d 502, 507 (3d Cir. 1988) (stating that a call options buyer is a purchaser of securities withstanding to pursue a misstatement claim against the issuer).

8. Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 585 F. Supp. 3d 405, 411–12 (S.D.N.Y. 2022), *cert denied*, No. 21 CIV. 761, 2022 WL 580787 (S.D.N.Y. Feb. 25, 2022) (establishing that the "[p]laintiff is a hedge fund" and that the "U.S. Spoofing Defendants" were market makers CIBC, TD Securities U.S., and Bank of America Merrill Lynch).

9. *See* Merritt B. Fox & Joshua Mitts, *Event-Driven Suits and the Rethinking of Securities Litigation*, 78 BUS. LAW. 1, 14, 78 (2023) (arguing that while "issuers that make misstatements must be subject to the threat of securities litigation that imposes damages liability on them . . . [t]he proper function, if any, of considering the price impact of [an eventual] corrective disclosure is to try to determine whether the misstatement had a meaningful inflationary effect on the issuer's share price in the first place. Often the corrective disclosure's price impact will not be helpful in this regard because some significant part of the drop is due to the fact that the news alleged to constitute the corrective disclosure has price-decreasing elements in it beyond the elimination of any misstatement-caused inflation. This problem is endemic with event-driven suits.").

10. Rule 10b-5 has long been understood as a tort claim. *See generally* Robert Thompson, *The Measure of Recovery Under Rule 10b-5: A Restitution Alternative to Tort Damages*, 37 VAND. L. REV. 349, 355 n.18 (1984).

11. *See, e.g.*, Complaint, SEC v. Left, No. 24-cv-06311, (C.D. Cal. Jul. 26, 2024) (asserting a claim against activist short publisher); Complaint, SEC v. Billimek, No. 22-cv-10542, (S.D.N.Y. Dec. 14, 2022) (stating a claim against traders); Complaint, SEC v. Constantin, No. 22-cv-04306, (S.D. Tex. Dec. 13, 2022) (asserting a claim against podcasters and social media users); Complaint, SEC v. Gu, No. 21-cv-17578, (D.N.J. Sept. 27, 2021) (making a claim against individual wash traders).

plaintiffs who are not shareholders, including short sellers,[12] issuers,[13] and traders in derivative securities[14] against a wide range of defendants, including corporate insiders,[15] analysts,[16] and market makers.[17]

The Supreme Court reiterated this tort-like conception of Rule 10b-5 claims in *Dura Pharmaceuticals v. Broudo* by citing the Restatement of Torts and an 1888 opinion on fraudulent misrepresentation (tort) claims.[18] To be sure, there is a wide-ranging debate in the literature as to whether fraud-on-the-market class actions reflect merely a form of deceit, a privately enforced statutory right to trade at accurate prices,[19] or a brand new kind of tort that has no comparable analog.[20] But all schools of thought view Rule 10b-5 as providing redress for injury between parties who are not in contractual privity with each other.

There is some historical fidelity to this conception. The standard out-of-pocket damages remedy under Rule 10b-5—which awards the plaintiff "the difference between the

12. *In re* Overstock Sec. Litig., No. 19-cv-709, 2020 WL 5775845, at *2 (D. Utah Sept. 28, 2020) ("Before the start of the class period at issue in this case, Plaintiff shorted more than 2.5 million Overstock shares. Plaintiff continued shorting Overstock shares throughout the class period. In fact, Plaintiff's only purchases during the class period were pursuant to preexisting contractual obligations owed to lenders whose stock Plaintiff had previously borrowed to sell short.").

13. ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 357 F. Supp. 2d 712, 714 (S.D.N.Y. 2005), *aff'd*, 493 F.3d 87 (2d Cir. 2007) (defendants "allegedly defrauded [plaintiff-corporation] into selling multiple series of [its convertible preferred] stock to entities [defendants] controlled or were controlled by.").

14. Set Cap. LLC v. Credit Suisse Grp. AG, 996 F.3d 64, 69 (2d Cir. 2021) (case based on allegation of market manipulation in an exchange-traded notes known as XIV notes, which "were a derivative financial product that increased in value when the market was calm and decreased in value when the market was volatile. The notes were issued by Credit Suisse and priced based on the inverse of a volatility index called the S&P 500 VIX Short-Term Futures Index (VIX Futures Index). This case concerns [plaintiff's] allegation that, after observing prior episodes of market volatility, Credit Suisse discerned an ability to depress prices for XIV Notes by purchasing VIX futures contracts on days when volatility spiked.").

15. Order Granting in Part and Denying in Part Plaintiff Littleton's Motion for Summary Judgment, *In re* Tesla, Inc. Sec. Litig., No. 18-cv-04865 (N.D. Cal. Apr. 1, 2022).

16. *In re* Salomon Analyst Metromedia Litig., 544 F.3d 474, 477–80 (2d Cir. 2008), *abrogated by* Amgen Inc. v. Conn. Ret. Plans & Tr. Funds, 568 U.S. 455 (2013) ("Plaintiffs allege that Grubman was an extremely influential [external] research analyst in the telecommunications sector, who could drive up share prices with positive recommendations . . . . We first address whether we should adopt a bright-line rule that bars application of the *Basic* presumption to a suit alleging misrepresentations by research analysts. Concluding that we should not, we next consider whether plaintiffs must make a heightened showing in a suit against research analysts to warrant the presumption. Concluding that they need not . . . .").

17. Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 585 F. Supp. 3d 405, 412 (S.D.N.Y. 2022).

18. Dura Pharms., Inc. v. Broudo, 544 U.S. 336, 343 (2005) ("Judicially implied private securities fraud actions resemble in many (but not all) respects common-law deceit and misrepresentation actions.") (citing Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975); L. LOSS & J. SELIGMAN, FUNDAMENTALS OF SECURITIES REGULATION 910–18 (5th ed. 2004); Restatement (Second) of Torts § 525 (AM. L. INST. 1977); S. Dev. Co. v. Silva, 125 U.S. 247, 250 (1888)).

19. Jill E. Fisch, *The Trouble with* Basic*: Price Distortion after* Halliburton, 90 WASH. U. L. REV. 895 (2013); Donald C. Langevoort, *Reading* Stoneridge *Carefully: A Duty-Based Approach to Reliance and Third-Party Liability Under Rule 10b-5*, 158 U. PA. L. REV. 2125, 2140–41, 2144 (2010).

20. For a comprehensive discussion of these possibilities, see John C.P. Goldberg & Benjamin Zipursky, *The Fraud-on-the-Market Tort*, 66 VAND. L. REV. 1755 (2013).

fair value of all that the [plaintiff] received and the fair value of what he would have received had there been no fraudulent conduct"[21]—was "borrowed from the common-law tort action of deceit" and "reflects the tort goals of compensating the injured party for harm and returning plaintiff to the position he occupied prior to the fraud."[22] It is rare to award injunctive or other equitable relief in Rule 10b-5 claims,[23] nor do they generally yield expectation damages as in a contract case.[24]

The tort-like nature of Rule 10b-5 is in some tension with the "contractarian theory" that has increasingly been employed to justify restrictions on Rule 10b-5 litigation, such as federal forum provision and mandatory arbitration clauses in corporate charters.[25] The logic of the contractarian theory goes something like this: when investors purchase shares in an initial public offering (IPO), they are aware of the provisions in the corporate charter and bylaws. Thus, purchasing the share reflects implicit assent to the terms in those charter and bylaws. The Delaware Supreme Court held as much in *Salzberg v. Sciabacucchi* when upholding a forum selection provision that required Securities Act claims be litigated in federal court: "corporate charters are viewed as contracts among the corporation's stockholders."[26] The same logic would seem to apply to a mandatory arbitration provision.[27]

But of course, when it comes to non-issuer defendants and non-shareholder plaintiffs, this logic breaks down. Whatever the merits of a contractarian theory of corporate law (which is hotly contested)[28], none of *these* parties sat at a proverbial bargaining table and

21. Acticon AG v. China N. E. Petroleum Holdings Ltd., 692 F.3d 34, 38 (2d Cir. 2012) (quoting Affiliated Ute Citizens v. United States, 406 U.S. 128, 155 (1972)).

22. Thompson, *supra* note 10, at 356–57.

23. *See* Nicholas R. Weiskopf, *Remedies Under Rule 10b-5*, 45 ST. JOHN'S L. REV. 733, 751–52 (1971) (noting that "a defrauded seller or purchaser will normally seek compensatory damages under 10b-5 rather than equitable relief.").

24. *See, e.g.*, Commercial Union Assurance Co. v. Ivan F. Boesky & Co., 824 F.Supp. 348, 350 (S.D.N.Y. 1993), *aff'd on other grounds*, 17 F.3d 608 (2d Cir.), *cert. denied*, 513 U.S. 873 (1994) ("The law does not furnish [benefit-of-the-bargain] damages under Section 10(b)."). *But see* Osofsky v. Zipf, 645 F.2d 107, 113 (2d Cir. 1981) (awarding expectation damages when the misstatement related to the terms of a merger and damages were not speculative). Decades ago, expectation damages were extended to common-law deceit actions so that contract plaintiffs are not left better off than tort plaintiffs. *See generally* Thompson, *supra* note 10, at 358.

25. A substantial recent trend in Delaware case law views corporate charters and bylaws as contracts. *See generally, e.g.*, Joseph A. Grundfest, *The Limits of Delaware Corporate Law: Internal Affairs, Federal Forum Provisions, and* Sciabacucchi, 75 BUS. LAW. 1319, 1358 (2020) ("[E]ven if an internal affairs standard is to be grafted onto the DGCL, FFPs would survive as valid charter provisions."); Dhruv Aggarwal, Albert Choi & Ofer Eldar, *Federal Forum Provisions and the Internal Affairs Doctrine*, 10 HARV. BUS. L. REV. 383, 388 (2020) (arguing that federal forum provisions should be "validated" through a more flexible internal affairs doctrine); *But see* Mohsen Manesh & Joseph A. Grundfest, *The Corporate Contract and Shareholder Arbitration*, 98 N.Y.U. L. REV. 1106 (2023) (mandatory arbitration provision for Rule 10b-5 claims would in principle be a contractarian question but would likely be invalidated as inequitable under Delaware corporate law though may be upheld in other states).

26. Salzberg v. Sciabacucchi, 227 A.3d 102, 135 (Del. 2020).

27. Manesh & Grundfest, *supra* note 25.

28. *See* Michael Klausner, *The Contractarian Theory of Corporate Law: A Generation Later*, 31 J. CORP. L. 779, 779 (2006) (claiming that "while the contractarian theory was a useful starting point for economic analysis of corporate law, more recent research demonstrates that as a description of reality, or a basis for policy prescription, the theory falls short."); Robert Anderson IV, *A Property Theory of Corporate Law*, 2020 COLUM. BUS. L. REV. 1, 21 (arguing that while the "move toward a contractarian theory is well established both in the academy and in the Delaware courts, where the most important corporate cases are decided . . . pure contractarian theory

negotiated anything with the issuer. It cannot possibly be said that the corporate charter reflects a contract between these parties. For this reason, it would be nonsensical to view the corporate charter as reflecting assent by parties who are not parties to the shareholder-issuer contract.

B. The Social Costs of Securities Fraud by Non-Issuers

While it is reasonable to expect that the social costs of securities fraud vary with the degree and magnitude of a given instance of fraud, there is no reason to expect that those costs turn on *who* the fraudster is. Due to space limitations, I will not provide a comprehensive overview of the social welfare effects of mispricing induced by fraud,[29] but they can be roughly summarized as distorting the allocation of real resources and reducing liquidity in the market. Any misstatement or omission that materially distorts a share price has these effects, so at least with respect to mispricing, it does not matter whether the misstatement is made by an issuer or a non-issuer. Neither does the direction of the distortion matter: artificially driving down a share price to induce investors to cash out at a deflated valuation has the same allocative and liquidity effects as inflating a price to induce investors to buy at an inflated valuation.

Several caveats are worth considering. For one, issuers may have a greater ability to affect share prices than non-issuers, because markets might rationally assume that issuers (and insiders) have more asymmetric information than non-issuers and thereby assign greater weight to a statement by an issuer. 'Company X is having a great quarter' means something different coming from the CEO compared to an analyst. Thus, the expected price impact of a misstatement—and thus its social cost—may be greater for issuers than non-issuers. However, that expected difference may be shrinking as recent years have shown that social media activists and meme-stock campaigns can send prices soaring and crashing.[30] In an era of AI-driven trading, it is not as clear that issuers move prices more than non-issuers.

The difference between issuers and non-issuers can also matter in other ways than the price. Corporate insiders may have private incentives to sell shares at inflated prices

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is difficult to square with basic principles of corporate law."); Martin Lipton & Steven A. Rosenblum, *A New System of Corporate Governance: The Quinquennial Election of Directors*, 58 U. CHI. L. REV. 187, 188 (1991) (arguing in the context of hostile takeovers, the contractarian view that "there is no basis for the assumption of intrinsic rights and entitlements in the corporate structure.").

29. For a comprehensive discussion see Marcel Kahan, *Securities Law and the Social Costs of "Inaccurate" Stock Prices*, 41 DUKE L.J. 977 (1992); *see also* Shikun Ke, The Social Welfare of Stock Market Mispricing (Mar. 12, 2024) (unpublished manuscript), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4644775 [https://perma.cc/N4GU-SRBA] (empirical analysis of stock mispricing, but not specifically on account of fraud).

30. Joshua Mitts, *Short and Distort*, 49 J. LEGAL STUD. 287, 288 (2020) ("[E]xamin[ing] 2,900 articles attacking mid- and large-cap firms published on the website Seeking Alpha and show[ing] that pseudonymous articles are followed by stock price declines and sharp reversals, leading to over $20.1 billion in mispricing."); Sue S. Guan, *Meme Investors and Retail Risk*, 63 B.C. L. REV. 2051, 2055–56 (2022) (explaining that "recent *meme investing* reveals the important but underappreciated way in which to-day's *retail investors* interact with and affect stock prices. Today's retail trades are increasingly sticky, or more likely to impact or predict future price movements—irrespective of their information content—as compared to idiosyncratic trades that tend to cancel each other out in aggregate. This is because today's retail traders are more numerous and coordinated than ever, have more direct market access, and use new, low-cost trading technology that promotes social aspects of trading.").

(whether directly on the open market or by having the issuer conduct offerings at inflated prices that finance private benefits of control) incentives that are lacking for non-issuers. The possibility that securities fraud can increase agency costs for public companies engaged in otherwise productive activities is a unique justification for issuer liability. That said, the aggregate impact of fraud by non-issuers may be greater because while there is only one issuer (and a handful of insiders) for any given security, there are many non-issuers—analysts, traders, message board participants, other companies, and so forth. Issuers and insiders face certain constraints on their ability to sell shares, including dilution considerations (for issuers) and reputational and legal restrictions on trading (for insiders). By contrast, non-issuers can often trade in and out of an entire position and thereby capture more of the gain from mispricing. Thus, while non-issuers may have a weaker incentive *individually* to commit securities fraud, in the *aggregate* non-issuer incentives may exceed those of issuers and insiders.

Here, again, the contractarian theory falls short. To be sure, to the extent that state corporate law upholds charter provisions as a kind of contract between shareholders and issuers,[31] market prices will reflect the value gains or losses arising from these (and any other) charter and bylaw provisions. With issuers having sold shares at a discount (or premium) *ex ante* based on these terms, it would be inequitable and (privately) inefficient not to enforce them *ex post*.[32] In efficient markets, the offering price thus provides a measure of investor protection.[33]

Of course, in social welfare terms, the offering price is inadequate, as was noted decades ago in the debates over mandatory disclosure and private ordering.[34] Because the social cost of asymmetric information generally exceeds the private cost, the "market price"

31. Stream TV Networks, Inc. v. SeeCubic, Inc., 279 A.3d 323, 354–55 (Del. 2022) (The court concluded "that the Charter provision and Section 271 [of the Delaware General Corporation Law] are materially different, we have not looked to Section 271 to interpret the Charter. And the parties have identified no public policy that would detract from our analysis of the Charter. Rather, enforcing the unambiguous Charter provision is consistent with our policy of seeking to promote stability and predictability in our corporate laws, and with recognition that Delaware is a contractarian state."); Manti Holdings, LLC v. Authentix Acquisition Co., 261 A.3d 1199, 1216–26 (Del. 2021) (holding that stockholders can voluntarily agree to waive their appraisal rights even though Section 262 of the Delaware General Corporation Law says any stockholder of Delaware corporation *shall* be entitled to an appraisal); New Enter. Assocs. 14, L.P. v. Rich, 295 A.3d 520, 574 (Del. Ch. 2023) (In stating the four-part test the court holds that "[t]he preceding tour through traditional fiduciary law, the DGCL, Delaware corporate law, and Delaware's support for private ordering indicates that the Covenant [not to sue] is not facially invalid. But to hold that stockholders in a Delaware corporation can commit not to sue for breach of fiduciary duty is a significant step, so it is worth considering other possible arguments against it. This section considers (i) whether the right to sue for breach of fiduciary duty is too big to waive, (ii) whether enforcing a provision like the Covenant threatens Delaware's corporate brand, (iii) whether upholding a provision like the Covenant collapses the distinction between corporations and LLCs, and (iv) the majority and dissenting opinions in *Manti*. Those considerations do not support declaring the Covenant facially invalid.").

32. Suppose, for example, that a mandatory arbitration provision would reduce firm value by $1 per share. Firm A adopts the provision while Firm B does not. If markets are efficient, Firm A's IPO price trades $1 lower than Firm B, so those purchasers are no worse off—the discount has compensated them for the value reduction.

33. This is indeed one shortcoming of Manesh & Grundfest, *supra* note 25, which does not consider whether market prices may render charter and bylaw arbitration provisions *ex post* fair.

34. *See* Merritt B. Fox, *Retaining Mandatory Securities Disclosure: Why Issuer Choice is Not Investor Empowerment*, 85 VA. L. REV. 1335, 1369 (1999) (stating that the current system of mandatory disclosure has decreased social welfare and describing the potential effects of the issuer choice regime on social welfare); Roberta

for charter provisions that increase asymmetric information is expected to be inadequate. The premium or discount applied to the market price by offering purchasers reflects the value of those charter provision(s) to those purchasers, but because those purchasers only pay a fraction of the social cost of asymmetric information, they will not rationally insist on compensation for those social costs.

This argument is even more compelling when considering Rule 10b-5 claims brought by plaintiffs other than shareholders against defendants other than issuers. Because these market participants lack governance rights, the price that emerges from shareholder-issuer bargaining is almost certainly going to fail to reflect those valuations. Suppose, for example, that a non-shareholder potential plaintiff would be willing to pay more than shareholders for a charter provision that does not limit Securities Act claims to federal court. In theory, an efficient bargain could be reached between the issuer, shareholders, and the potential plaintiff which 'divides the surplus', *i.e.*, makes the issuer better off (by increasing the offering price), the shareholder better off (by providing a transfer payment from the potential non-shareholder plaintiff), and the non-shareholder plaintiff better off (by yielding an increase in utility that exceeds the transfer payment). But because non-shareholder plaintiffs are generally not participating in that 'negotiation' (either by setting the price or negotiating for non-price terms in some other way), that bargain will not emerge. And this is true even if the social cost of charter provisions is equal to the private cost.

III. NON-ISSUER PRIVATE SECURITIES LITIGATION IN THE COURTS

A. Private Litigation Against Tweeters and Their Like

The rise of securities fraud cases against non-issuers is largely a technological story. As I noted five years ago,[35] social media and algorithmic trading have created new ways to move share prices rapidly, often as simple as sending out a tweet. In fact, one of the early non-issuer private securities class actions was brought against Elon Musk for his infamous 2018 tweet suggesting that funding was secured to take Tesla private.[36] While Elon ultimately prevailed at trial on materiality and reliance (in one of the rare securities fraud

Romano, *Empowering Investors*: *A Market Approach to Securities Regulation*, 107 YALE L.J. 2359, 2377 (1998) (describing how social welfare is reduced in the market).

35. Joshua Mitts, *A Legal Perspective on Technology and the Capital Markets: Social Media, Short Activism and the Algorithmic Revolution* (Colum. L. & Econ., Working Paper No. 615, 2019), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3447235 (on file with the *Journal of Corporation Law*).

36. Consolidated Complaint for Violations of the Federal Securities Laws, *In re* Tesla, Inc. Sec. Litig., No. 18-cv-04865, (N.D. Cal. Jan. 16, 2019). For an extended discussion of the private litigation against Elon Musk see David Rosenfeld, *Elon Musk and the Virtues of Restraint*, 53 STETSON L. REV. 307, 331–32 (2024) (explaining that "after denying the motion to dismiss, the judge granted the plaintiffs summary judgment on two important issues: the falsity of the statements and scienter . . . . [T]he case ended up going to trial over the issue of materiality, but that allowed for testimony over the same facts that go to scienter, and the testimony showed that there were plenty of disputed issues of material fact on that score . . . . The issue before the jury was one of materiality rather than scienter—that issue having been decided by the judge – but the two issues melded together, and the same evidence that came in for materiality also went to scienter. In the end, the jury determined that whatever misstatements there may have been were immaterial, but in a way, they were also saying that whatever Musk did, he didn't act with an intent to deceive or defraud.").

cases that actually went to trial),[37] the class was certified and the court entered a judgment for the plaintiffs on the issue of falsity and scienter—making it one of the first procedurally successful securities class actions against a non-issuer for making a material misstatement under Rule 10b-5.[38]

The controversy over Musk's 2018 tweet that ultimately led to a private class action first found its way to Musk in the form of an enforcement action, the settlement of which led to the famous "Twitter sitter."[39] In fact, the SEC and DOJ have pursued a series of enforcement actions in recent years against tweeters and social media fraudsters. Some of these involved corporate insiders seeking to drive up the share price of the issuer. In one case (in which I testified for the U.S. government), the defendant "used aliases to post positive messages about [the issuer]'s business and operations on investor message boards, in order to artificially increase and maintain the share price of [the issuer's] securities."[40] In another case, the defendant, who was not a corporate insider, "falsely posted on iHub about his trading plans and position with regard to [the issuer's] stock," claiming that his shares were "locked up" while on the same day selling 300,000 shares.[41] The defendant also "placed 'spoof' orders to buy 2,000,000 shares at prices away from the best bid with the intent to cancel" while posting message board posts concerning those bids that were misleading because he "never acknowledged that he was, in fact, the one who had submitted the bids or that he intended to cancel those orders before execution."[42]

While frauds by shallow-pocketed fraudsters like these may be unlikely to lead to private class actions, they sometimes do. In one case, investors sued Ryan Cohen, an activist investor who had acquired a stake in Bed Bath & Beyond, for engaging in a pump-and-dump scheme.[43] The core allegations were simple: in response to a negative article about the Company on CNBC, Ryan Cohen posted a tweet with a smiley moon emoji.[44] "[A]ccording to Plaintiff, Cohen was telling his hundreds of thousands of followers that Bed Bath's stock was going up and that they should buy or hold. They did so, sending the price soaring."[45] Days later, Cohen filed a Form 13D which did not disclose any intention

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37. CORNERSTONE RSCH., SECURITIES CLASS ACTION FILINGS: 2022 MIDYEAR ASSESSMENT, https://securities.stanford.edu/research-reports/1996-2023/Securities-Class-Action-Filings-2023-Year-in-Review.pdf [https://perma.cc/8FYJ-NVE3] (between 1996 and July 2022 "there have been only 23 securities fraud cases that have gone to trial, and only 17 that have reached a full or partial verdict.").

38. Order Granting in Part and Denying in Part Plaintiff Littleton's Motion for Summary Judgment, *supra* note 15.

39. Complaint, SEC v. Musk, No: 18-cv-08865 (S.D.N.Y. Sept. 27, 2018) (This action resulted in a settlement requiring that, among other things, "Tesla will establish a new committee of independent directors and put in place additional *controls and procedures to oversee Musk's communications*"); Press Release, SEC, Elon Musk Settles SEC Fraud Charges; Tesla Charged with and Resolves Securities Law Charge (Oct. 2, 2018), https://www.sec.gov/newsroom/press-releases/2018-226 [https://perma.cc/G6FJ-RP2H] (emphasis added).

40. Indictment at 4, United States v. Berman, No. 20-cr-00278 (D.D.C. Dec. 15, 2020).

41. Information at 3, United States v. Nielsen, No. 22-cr-00161(N.D. Cal. Apr. 18, 2022).

42. *Id.* at 3–4.

43. Investors also sued the Company and its CEO for a related statement it had made, which the court dismissed, finding that the statement was not false, misleading, or otherwise actionable. *In re* Bed Bath & Beyond Corp. Sec. Litig., 687 F. Supp. 3d 1, 9 (D.D.C. 2023).

44. *Id.* at 7.

45. *Id.*

to sell, and a Form 144 which "outlined his *potential* plan to sell stock."[46] The price remained high, and at roughly the same time, Cohen secretly sold his entire stake to yield $68 million in profit.[47]

In denying Cohen's motion to dismiss the complaint, the court found that "[t]he moon-emoji tweet was plausibly misleading because it was perceived 'as a rallying cry to buy Bed Bath's stock,' even though Cohen had soured on Bed Bath."[48] Cohen tried to advance an alternative interpretation for his sales, namely, that "[h]e 'decided to exit his position when the price unexpectedly increased to a value that exceeded what he believed it was worth.'"[49] The court was unimpressed, concluding that it is a "stretch" to conclude that Cohen only formulated a desire to sell after the price surged.[50] In another case, the court similarly held that private plaintiffs stated a claim for securities fraud under Rule 10b-5 when Elon Musk failed to disclose his "activist intentions and ownership" of Twitter on Form 13D.[51] While Musk would later go on to purchase Twitter in an acquisition, at that time he was not a Twitter insider, and Twitter was not a defendant.

These cases reflect an emerging focus by private plaintiffs on misleading statements—such as social media posts or other commentary—by non-issuers. Just as regulatory and enforcement actions continue in this area,[52] so does private litigation.

B. Market-Manipulation Claims Under Rule 10b-5

Another type of case where non-issuer defendants are sued for violations of Rule 10b-5 is market manipulation. These cases were traditionally quite difficult for private plaintiffs to bring. The high watermark of judicial skepticism was reached in the Second Circuit's 2007 opinion in *ATSI v. Shaar Fund*, that rejected a claim that short sellers manipulated the market in a firm's shares based on general allegations of high-volume selling and price declines lacking a causal connection to the selling.[53] The court held that "a manipulation complaint must plead with particularity the nature, purpose, and effect of the fraudulent conduct and the roles of the defendants."[54] Similar cases from that era showed substantial skepticism toward assertions of manipulative purpose in otherwise legitimate trading. For

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46. *Id.*

47. *Id.* at 8.

48. *In re Bed Bath & Beyond*, 687 F. Supp. 3d at 11. The court reached a similar conclusion regarding the Form 13Ds filed by Cohen that failed to disclose his plan to sell shares, and rejected Cohen's argument that Form 13D cannot form the basis of a Rule 10b-5 claim. *Id.* at 13–14. The court also found that the Form 144 was misleading by failing to disclose the planned sale. *Id.* at 14–15.

49. *Id.* at 15.

50. *Id.* at 15–16.

51. Okla. Firefighters Pension & Ret. Sys. v. Musk, No. 22-cv-03026, 2023 WL 6393865, at *8 (S.D.N.Y. Sept. 29, 2023).

52. *See* Indictment at 4, United States v. Left, No. 24-cr-00456 (C.D. Cal. July 25, 2024) (describing how Left "manipulate[d] the price of a Targeted Security" which allowed him to profit "from his advance[d] knowledge"); Complaint at 5, SEC v. Left, No. 24-cv-06311, (C.D. Cal. July 26, 2024) ("This civil enforcement action concerns Left's misuse of the Citron Research platform in connection with reports and tweets he published between approximately March 2018 to December 2020 (the "Relevant Period") relating to 23 target companies on at least 26 separate occasions which allowed him to generate approximately $20 million in illegal trading profits through a scheme to defraud.").

53. ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 493 F.3d 87, 99–104 (2d Cir. 2007).

54. *Id.* at 102.

example, in a 2010 opinion, *Cohen v. Stevanovich*, the Southern District of New York rejected a claim that non-issuer defendants engaged in so-called "naked short selling," *i.e.*, short selling without borrowing the underlying shares for delivery, which "supposedly created 'phantom shares' of [the issuer] stock and caused the number of shares of [the issuer] that are beneficially owned to exceed the number issued by the Company."[55]

During the 2010s, this trend began to shift. A key turning point was *Sharette v. Credit Suisse*, in which Credit Suisse allegedly orchestrated an offering of floorless convertible notes:

> [F]or the purpose of allowing their hedge fund clients to make huge profits while sinking the price of [the issuer's] stock, hid this purpose from [the issuer] and its investors, and then intentionally lent out far more shares of common stock for short sales than was necessary for investors to "hedge" their positions in [the issuer]'s convertible notes, facilitating the market manipulation—and depression—of [the issuer]'s stock price.[56]

Credit Suisse did not issue the convertible notes, nor was Credit Suisse the issuer of the shares subject to conversion.[57] Rather, plaintiffs alleged that Credit Suisse—a third-party non-issuer defendant—manipulated the issuer's share price.[58] The court held that these facts were sufficient to state a claim for a violation of Rule 10b-5.[59]

In 2021, the Second Circuit weighed in again on market manipulation claims under Rule 10b-5 in *Set Capital v. Credit Suisse*.[60] This securities class action involved allegations of market manipulation in an exchange-traded note known as XIV, a volatility derivative that tracked the inverse of the VIX volatility index.[61] The plaintiffs alleged that Credit Suisse:

> [M]anipulated the market by issuing millions of additional XIV Notes knowing or recklessly disregarding the virtual certainty that their own hedging activity would trigger a liquidity squeeze in VIX futures contracts, destroy the value of XIV Notes, and allow Credit Suisse to accelerate and redeem the notes at a substantial loss to investors while locking in a profit for its own account.[62]

To be sure, *Set Capital* involved an issuer defendant and contained a misrepresentation claim alongside the manipulation one.[63] But *Set Capital* has emerged as a notable development in non-issuer securities fraud cases, not for the doctrine it espoused—much of which was quoted straight from *ATSI*—but for the way that doctrine was applied. Criti-

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55. Cohen v. Stevanovich, 722 F. Supp. 2d 416, 421–22 (S.D.N.Y. 2010).

56. Sharette v. Credit Suisse Int'l, 127 F. Supp. 3d 60, 82–83 (S.D.N.Y. 2015).

57. *Id.* at 73–74.

58. *Id.* at 73.

59. *Id.* at 81. Like most securities fraud cases brought under Rule 10b-5, *Sharette* settled after the motion to dismiss.

60. *See generally* Set Cap. LLC v. Credit Suisse Grp. AG, 996 F.3d 64, 76 (2d Cir. 2021) (discussing the market manipulation of investment vehicles called XIV Notes).

61. *Id.* at 69–70.

62. *Id.* at 76.

63. *Id.* at 82.

cally, in *Set Capital*, plaintiffs had not alleged any "smoking gun" evidence of communications or emails that indicated a manipulative purpose. Rather, the Second Circuit drew an inference of manipulative intent from the data:

> Open-market transactions that are not inherently manipulative may constitute manipulative activity when accompanied by manipulative intent. In some cases, as here, "scienter is the only factor that distinguishes legitimate trading from improper manipulation." To the extent Credit Suisse claims it hedged for a legitimate purpose, its position contradicts the complaint.[64]

Courts' willingness to infer a manipulative purpose from trading data represented a substantial step forward in allowing plaintiffs to bring Rule 10b-5 manipulation cases against non-issuers.

Less than one year after *Set Capital*, the Southern District of New York embraced this data-driven approach to market manipulation litigation in *Harrington v. CIBC*.[65] In that matter, the plaintiff sued three market makers: CIBC, TD Securities, and Bank of America/Merrill Lynch for spoofing the shares of Concordia, a dual-listed Canadian company whose shares traded in Canada and the United States.[66] Like *Set Capital*, the *Harrington* court denied the defendants' motion to dismiss a complaint that alleged spoofing activity based solely on data-driven indicia.[67] And these defendants were not market makers. The same court subsequently held that broker-dealers could be held primarily liable under Rule 10b-5(a) and (c) for spoofing activity by customers.[68] With the exception of loss causation, courts have generally upheld spoofing complaints based on similar data analysis.[69] Loss causation poses unique but not insuperable complexities when it comes to high-frequency market manipulation, and is the subject, particularly as concerns pleading long-term price impact, of additional briefing in these cases at this time.[70]

64. *Id.* at 77–78 (emphasis added) (quoting ATSI Commc'ns, Inc. v. Shaar Fund, Ltd., 493 F.3d 87, 102 (2d Cir. 2007)).

65. Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 585 F. Supp. 3d 405 (S.D.N.Y. 2022), *reconsideration denied*, No. 21 CIV. 761, 2022 WL 580787 (S.D.N.Y. Feb. 25, 2022).

66. *Id.* at 411.

67. *Id.* at 417 (explaining how courts "examine (1) the passage of time between placement and canceling of orders (usually in milliseconds), (2) cancellation of orders when large baiting orders are partially filled or legitimate small orders are completely filled, (3) parking baiting orders behind smaller legitimate orders placed by other traders and (4) large disparities in the volume of baiting orders on one side of the market and legitimate orders placed by the spoofer.").

68. *See* Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., No. 21 CIV. 761, 2023 WL 6316252, at *7 (S.D.N.Y. Sept. 28, 2023) (discussing that there can be "primary liability for a broker recklessly acting on behalf of a manipulative client").

69. *See* Nw. Biotherapeutics, Inc. v. Canaccord Genuity LLC, No. 22-CIV-10185, 2023 WL 9102400 (S.D.N.Y. Dec. 29, 2023), report and recommendation adopted sub nom (upholding spoofing complaint based on data analysis); Nw. Biotherapeutics, Inc. v. Canaccord Genuity LLC, No. 22-cv-10185, 2024 WL 620648 (S.D.N.Y. Feb. 14, 2024); Phunware, Inc. v. UBS Sec. LLC, No. 23 CIV. 6426, 2024 WL 1465244 (S.D.N.Y. Apr. 4, 2024).

70. Plaintiff in *Nw. Biotherapeutics*, following the Court's Report and Recommendation in the 2023 *Harrington Glob.* case, filed an amended complaint with an expanded repleading on loss causation. Second Amended Complaint at 90–109, Nw. Biotherapeutics, Inc. v. Canaccord Genuity LLC, No. 22-CIV-10185 (S.D.N.Y. Mar. 18, 2024). In the subsequent January 2025 Report and Recommendation on Defendants' motion to dismiss Plain-

IV. THE FUTURE OF NON-ISSUER SECURITIES LITIGATION: CHALLENGES AND OPPORTUNITIES

Subject to the space constraints of this symposium piece, I will sketch out three challenges for private securities litigation as plaintiffs seek to move beyond issuer defendants.

Reliance. Many non-issuer claims consist of schemes to defraud.[71] Since the Supreme Court's 2019 decision in *SEC v. Lorenzo*, it is clear that fraudulent schemes can be pursued under subsections (a) and (c) to Rule 10b-5, and do not require that the defendant "made" a misstatement in violation of subsection (b).[72] But the Court has not revisited its 2008 decision in *Stoneridge*, which precluded reliance on "hidden" fraud.[73] The fraud-on-the-market presumption of reliance set out in *Basic v. Levinson* and reaffirmed in *Halliburton II* presupposes that false information was injected into the market *by the defendant* and

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tiff's Second Amended Complaint, with the expanded repleading on loss causation, the court in *Nw. Biotherapeutics* held that the Second Amended Complaint "sufficiently pleads loss causation with respect to the approximately 40 million shares of stock sold by [Plaintiff] at prices derived from closing prices on dates when Spoofing Episodes occurred", as Plaintiff's expanded pleading included the identification and presentation of both cash sales and exchange agreement sales whose price conversion formulae included the closing price on dates on which alleged spoof episodes occurred which, the court held, "sufficiently pleads the [required] *formulaic connection* between [Plaintiff's] stock sales, the Pricing Dates [for the sales], and Defendants' spoofing." Nw. Biotherapeutics, Inc. v. Canaccord Genuity LLC, No. 22-cv-10185, 2025 WL 368717, at *7, 21 (S.D.N.Y. Jan. 31, 2025) (emphasis added). The court, however, also held that the Second Amended Complaint "fails to sufficiently plead a long-term, persistent negative impact on [Northwest Biotherapeutic's] stock price, requiring dismissal of Plaintiff's claims relating to the approximately 234 million [shares of Northwest Biotherapeutic stock not sold pursuant to pricing formulae which included the closing price of dates on which spoofing episodes occurred]." *Id.* at *21. On the question of long-term price impact, Plaintiff has filed a limited objection to the court's January 2025 Report and Recommendation "regarding only whether Plaintiff sufficiently pleaded loss causation for Plaintiff's sales that took place more than one-day after Defendants engaged in manipulative spoofing." *See* Plaintiff's Limited Objection at 1, Nw. Biotherapeutics, Inc. v. Canaccord Genuity LLC, No. 22-cv-10185 (S.D.N.Y. Feb. 14, 2025). Similarly, Plaintiff in *Phunware*, following the Court's Opinion and Order on Defendants' Motion to Dismiss in the 2023 *Harrington Glob.* case, filed a letter motion seeking leave to file an amended complaint repleading loss causation. Letter Motion, Phunware, Inc. v. UBS Sec. LLC, No. 23-cv-6426 (S.D.N.Y. Apr. 17, 2024). In its November 2024 Opinion and Order, the court in *Phunware* held that Plaintiff's loss causation allegations in its proposed amended complaint, which included Plaintiff identification and presentation of sales that it made "within seconds of Defendant's spoofing activity," "had sufficiently alleged loss causation under the temporal proximity theory." Phunware, Inc. v. UBS Sec. LLC, No. 23-cv- 6426, 2024 WL 4891891, at *2 (S.D.N.Y. Nov. 26, 2024). Further, the court in *Phunware* held that "because Plaintiff sufficiently pleads loss causation under the temporal proximity theory, the Court concludes that leave to amend is proper. At this stage . . . it unnecessary to determine whether the Plaintiff sufficiently pleads long-term price impact." *Id.* at *3.

71. *E.g.*, Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 585 F. Supp. 3d 405, 415 (S.D.N.Y. 2022) (The scheme allegedly entailed "U.S. and Canadian Spoofing Defendants perpetrat[ing] a spoofing scheme to drive down Concordia's share price for the purpose of purchasing Concordia's shares at lower prices. The scheme was carried out by the simultaneous entry of large quantities of orders to sell by a U.S. Spoofing Defendant and its Canadian affiliate."); Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 21-cv-761, 2023 WL 6316252, at *8 (S.D.N.Y. Sept. 28, 2023) (Second Amended Complaint "alleges that Defendants derived economic gain from the spoofing scheme through."); Complaint at 5, SEC v. Left, No. 24-cv-06311 (C.D. Cal. July 26, 2024) ("This civil enforcement action concerns Left's misuse of the Citron Research platform in connection with reports and tweets he published between approximately March 2018 to December 2020 (the "Relevant Period") relating to 23 target companies on at least 26 separate occasions which allowed him to generate approximately $20 million in illegal trading profits through a scheme to defraud.").

72. Lorenzo v. SEC, 587 U.S. 71, 83 (2019).

73. *See* Langevoort, *supra* note 19 (discussing the *Stoneridge* case).

affected the market price as a result.[74] Like many other non-issuer actions, *Lorenzo* was a governmental enforcement action, so reliance was irrelevant.[75] But private plaintiffs will have a difficult time pursuing non-issuer claims against participants in deceptive and fraudulent schemes—like hedge funds collaborating with social media posters—who themselves are not lying to the public. Similar challenges are posed by so-called "fraud on the broker" cases where the false statement is made to a broker-dealer "in connection with" the purchase or sale of a security but is not publicly disseminated in the market.[76]

Loss causation and damages. A unique challenge with market-manipulation claims that do not involve false "statements" in the traditional sense is determining the duration of the price impact of the alleged manipulation.[77] In a garden-variety misstatement case, the distortive effect is measured either at the time of the misstatement (*i.e.*, for an inflationary misstatement, a price increase) or at the time of a "corrective disclosure" that reveals the falsity of the misstatement to the market (*i.e.*, for an inflationary misstatement, a price decline). But it can be difficult to identify a corrective disclosure for a price-distorting manipulative practice, especially for practices involving repeated instances of high-frequency manipulation like spoofing. Spoofers do not typically announce that a baiting order was fraudulent, which would cause the price to revert to a non-manipulated level. For this reason, estimating the duration of the price impact of manipulation must rely on economic analysis, or when such analysis is unavailable—like at the pleading stage of a case—on judicially derived 'rules of thumb.'

There has been an evolution in the case law on this issue. In *Harrington*, the first spoofing case in the Southern District of New York to survive a motion to dismiss, the Court held that it was sufficient for plaintiffs to allege that "[w]hen the spoofing events

74. *See generally* Basic Inc. v Levinson, 485 U.S. 224 (1988); *see also* Halliburton Co. v. Erica P. John Fund, Inc., 573 U.S. 258 (2014).

75. *Lorenzo*, 587 U.S. at 71.

76. *Cf.* SEC v. Hwang, 692 F. Supp. 3d 362, 371 (S.D.N.Y. 2023) (alleging the owner and employees of Archegos Capital "engaged in a fraudulent scheme to manipulate the market for certain securities and to deceive Archegos's *swap counterparties* about the riskiness of its overall investment portfolio. The effect of this alleged scheme was to artificially inflate the price of those securities, to induce the counterparties to execute further swaps, and to avoid margin calls from the counterparties, all to the benefit of Archegos.") (emphasis added); Graham v. SEC, 222 F.3d 994, 1001–02 (D.C. Cir. 2000) (affirming an SEC order which concluded trades "constituted a fraud under section 10(b) and Rule 10b-5 . . . [because the trader] defrauded the broker-dealers through which he traded by causing them to remit sales proceeds to him that they would not have paid had they known the true nature of the transactions", and rejecting petitioner's argument that a "fraud must [be] perpetrated upon an actual or potential investor [and that since] the brokers were never parties to the securities transactions, but merely executed them . . . no violation of section 10(b) was possible.") (internal quotations omitted). The Supreme Court has also specifically addressed the applicability of Section 11 fraud claims to fraud against brokers. United States v. Naftalin, 441 U.S. 768, 770 (1979) ("The question presented in this case is whether § 17(a)(1) of the Securities Act of 1933 . . . prohibits frauds against brokers as well as investors. We hold that it does.").

77. To be sure, spoofing can be thought of as sending a false statement regarding a genuine intent to execute baiting orders. *See* United States v. Coscia, 866 F.3d 782, 797 (7th Cir. 2017) (spoofing-defendant's "scheme was deceitful because, at the time he placed the large orders, he intended to cancel the orders."); United States v. Smith, 555 F. Supp. 3d 563, 574, 576 (N.D. Ill. 2021) (holding that "[s]poofing can constitute misrepresentation by creating illusory market movement through the injection of false information into the market" and thus that the indictment against spoofing-defendant "adequately allege[d] that the Defendants actively concealed, through [spoofing], material information from the marketplace; namely, that the perceived market movement was in fact caused by large orders placed with the intent to cancel them."). However, there is never a corresponding "corrective disclosure" that reveals the false nature of those baiting orders.

occur continuously throughout the day and continue without interruption over a protracted period of time, the long-term cumulative effect of spoofing places enormous downward pressure on the market price of a security."[78] This Court rejected the notion that "individual spoofing events cannot have a long-term cumulative effect on the price of a stock" and held that "[w]hether the effects of the alleged market manipulation dissipated is a question of fact that can be answered only upon a more fully developed record."[79]

Shortly after *Harrington*, the Second Circuit decided *Gamma Traders v. Merrill Lynch*, a private commodities spoofing case.[80] In *Gamma Traders*, the plaintiffs alleged that they suffered losses because they traded on the same days as spoofing episodes.[81] The Second Circuit rejected these allegations as excessively broad, holding that plaintiffs must allege specific facts which "justify an inference that the market price was still artificial" at the exact time of the transactions.[82] Alternatively, plaintiffs may allege trades that were "so close in time to Defendants' spoofing" that the court may "infer as a matter of common sense that the market prices were artificial" at the time of the plaintiffs' trades.[83] While loss causation was not at issue in *Harrington II*, it came up again in two recent spoofing opinions: *Nw. Biotherapeutics* and *Phunware*.[84] In both cases, plaintiffs were forced to replead loss causation with a high degree of quantitative specificity to show that the price was still affected by the defendants' spoofing activity.[85] The challenge of price impact is likely to remain a daunting one for spoofing plaintiffs going forward.

Truth on the market (or reliance revisited). A broader question for non-issuer cases goes to the very core of what securities fraud is. A refrain typically heard among defense counsel is that non-issuer cases depart from the traditional goal of the securities laws to "protect investors" from deceptive issuers lying to raise capital and amount to efforts to regulate practices that everyone knows are occurring on Wall Street. For example, if the market knows that short sellers are closing their positions following activist reports, is there still deception in statements to the contrary? If investors understand that orders may be canceled, are they still harmed by spoofing?

A full economic analysis of the relationship between investor expectations and harm from fraud is beyond the scope of this essay. I would only note that at the time the securities laws were enacted, it was also understood that fraud was widespread. The presence of fraud in a market harms investors by increasing bid/ask spreads, driving a wedge between project valuations and the prices those projects can command in the market. The same holds for non-issuer fraud. Merely because a practice is commonplace on Wall Street does not mean it is socially harmless. Just as fraud does not stop with issuers, neither should private securities litigation.

78. Harrington Glob. Opportunity Fund, Ltd. v. CIBC World Mkts. Corp., 585 F. Supp. 3d 405, 419 (S.D.N.Y. 2022).

79. *Id.* at 419–20.

80. Gamma Traders - I LLC v. Merrill Lynch Commodities, Inc., 41 F.4th 71 (2d Cir. 2022).

81. *Id.* at 74.

82. *Id.* at 80.

83. *Id.*

84. *See* cases cited, *supra* note 70.

85. *Id.*